Vol. VII, No. 5 August 1996

Strategic Imperatives for EDS

Exhibit 1

EDS - STRATEGIC DIRECTIONS

- Target high margin international contracts
- Emphasize A.T. Kearney consulting
- Seek sub-$200m contracts
- Partner with telecom operator

Source: INPUT

Analysis of EDS' Q2 results and management review, presented on July 16, 1996, reveals four key elements to EDS' strategic direction (see Exhibit 1):

- EDS will target international contracts, because ~~that~~ these contracts are characterized by less competition and higher margins. Privatization and strong outsourcing demand are driving these opportunities, particularly in Europe. EDS is likely to target the large amount of outsourcing revenues available from the UK Government, which CFO Jody Grant estimates to be potentially $10B over the next year.
- EDS will also emphasize its consulting business: here, too, the strategic reason is because consulting yields relatively high margins. EDS' acquisition of A.T. Kearney in 1995 has strengthened this business for EDS significantly.
- EDS will seek out contracts with total revenues of under $200M, particularly overseas, because these contracts are more lucrative than the megacontracts, which are characterized by intense competition, and in the case of U.S. Federal contracts, narrow margins.
- A continuing goal appears to be a partnership (non-exclusive) with a telecommunications company. This would position EDS to provide network-based services, leveraging an outsourcing segment of strong growth, and enable EDS to offer a broader continuum of services to future customers. Such a partnership, according to Grant, might involve reciprocal IT and network services between the two partners as well as their joint marketing of comprehensive, integrated offerings to outside customers. EDS may view such a partnership as a means to strengthen its Internet/intranet service offerings as well.

- EDS plans to increase investment in the training of its staff in client-server computing. EDS will also increase spending on advertising to promote itself as an independent company open to new partnerships as well as one that improves the productivity of its customers.

- EDS may move its Electronic Commerce organization, currently horizontally-based under a vertical SBU. INPUT believes that a likely place for this group would be Barry Sullivan's Internet & New Media SBU, ~~which is under the Communications Industry Group~~.

Financial data and new contract information are included on the following pages.

Financial Overview

- EDS' Q2 operating revenues were up nearly 19%, while net income increased nearly 9% to $246.6M, before adjusting for split-off-related charges. Due to these charges, EDS reported a Q2 net loss of $326.5M.

- A few clients with financial problems, such as Spectradyne, which is in bankruptcy, negatively affected Q2 revenues.

- While costs of the split-off from GM have depressed operating margins somewhat (11.6% as compared to 12.6% in 1995), gross margins are actually up. Operating margins are expected to regain their 12% levels in 1997.

- EDS' large contract backlog of $76.6B is a stabilizing influence on these margins. GM's portion of the backlog, currently in, $36.8B, will diminish now that EDS has become an independent company. EDS' debt, used to pay the dividend to GM, has increased from $370M to $2.7B.

- EDS is working on reducing its G&A expenses, which were running at 12% three to four years ago, and were brought down to 8.8% during Q2.

New Contracts

- EDS won $1.536B in contract awards in Q2 1996. This total revenue represents 44 deals, none in excess of $200M, with about half coming from contracts under $100M. EDS views this as a positive trend due to the higher margins on these smaller contracts.

- Of the 44 contracts won during Q2, 21 were U.S. and 23, international.

- Recent contracts highlighted during EDS' announcement included EDS' recent desktop services outsourcing contract with Citibank, which has a value of $240M and a duration of 3 years, and a multimillion retail contract with Kellwood, a marketer and manufacturer of apparel. The latter is an example of CoSourcing, which EDS defines as a "collaborative, value-enhanced service that focuses on improving the business performance of customers as measured by agreed-upon business metrics."

- During the first two weeks of July, EDS signed another $800M in new business.

- EDS projects that its revenues from consulting (resulting from both the A.T.Kearney acquisition and EDS' other consulting services) will total about $750M for 1996. These revenues tend to be characterized by higher margins.

The Q2 geographic revenue breakdown is indicated in Exhibit 2.

Exhibit 2

Q2 Geographic Revenue Shares

Region	% of Total Rev~~.~~enue
U.S.	71%
Europe	21%
Other (non-U.S.)	8%

Source: EDS

- Base business revenues grew 24.6%, boosted by strong growth in Asia (up 71%) and Europe (56%). The growth surge in the Asia-Pacific region, as compared to 33% during Q1, reflects new revenues from EDS' South Australia contract.

- Q2 revenue growth was very strong in the Government sector, boosted by contracts with foreign governments which have higher margins. Key sector revenue growth rates are indicated in Exhibit 3.

Exhibit 3

Q2 Sector Growth

Sector	Q2 % Change
Government	41%
Finance	27%
Communications	20+%
Manufacturing	16%

Source: EDS

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- TARGETING HIGH MARGIN INTERNATIONAL CONTRACTS
- EMPHASIS ON A.T. KEARNEY CONSULTING
- EMPHASIS SWITCHES TO SUB-$200M CONTRACTS
- PARTNERING WITH TELECOM OPERATOR

lower cost getting

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Exhibit 3 Q2 Sector Growth

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SECOND QUARTER

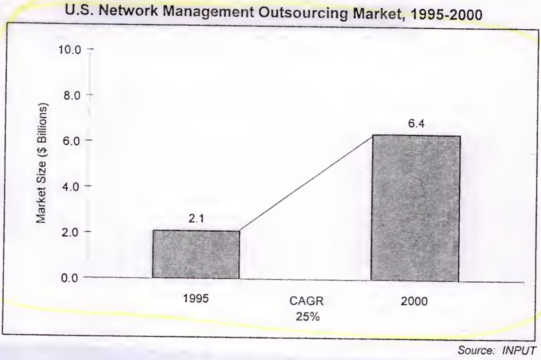
~~NEW~~ NETWORK MANAGEMENT OUTSOURCING CONTRACTS

STRONG GROWTH MARKET

Analysis of INPUT's Outsourcing Database for the Second Quarter of 1996 indicates that Network Management Outsourcing is increasing, and that many of the very large contracts include network management outsourcing as a key component.

EXHIBIT 1:

Exhibit 1



Drivers of Network Management Outsourcing growth include:

- Trend toward distributed computing
- Increasing complexity and maintenance requirements of networks
- Increasing dependence on networks for mission-critical activities
- Soaring support costs

SIGNIFICANT Q2 CONTRACTS

A sampling of notable Network Management Outsourcing contracts won during the Second Quarter of 1996 appears in Exhibit 2, followed by a brief description of key contracts.

EXHIBIT 2

SIGNIFICANT NETWORK MANAGEMENT OUTSOURCING CONTRACTS AWARDED DURING Q2

Vendor	Customer	Industry	Value ($M)	Length
AT&T Solutions	Mastercard International	Finance	NA	5
AT&T Solutions	Merrill Lynch	Finance	500	6
EDS	Automakers Ltd (S. Africa)	Disc. Mfg	22.7	10
Hewlett-Packard	Groupo Proeza (Mexico)	Disc Mfg	NA	5
Hewlett-Packard	China Commodity Exchange	Finance	NA	1
Hewlett-Packard	SmithKline Beecham	Proc. Mfg.	1	3

All of these contracts reflect the influence of globalization, a key driver in the Network Management Outsourcing market. Several contracts are capsulized below.

AT&T Solutions/Mastercard International:
This is a multimillion dollar contract to design, build and support the management of a global transaction processing network for Mastercard so that it will be able to support credit and debit transactions in more than 30 countries. AT&T will support end-to-end network management and provide maintenance of customer premises equipment, as well as program and network engineering management. AT&T will leverage its WorldSource services and its global frame relay service. It will deliver services through its new Global Client Support Center in Durham, N.C., linked to regional centers in Singapore and Amsterdam. The contract is indicative of the need of financial players to develop strong electronic commerce capabilities in order to remain competitive in the Finance sector.

AT&T Solutions Merrill Lynch:
AT&T and Merrill Lynch formed a strategic alliance to provide and manage networking capabilities for Merrill Lynch's Trusted Global Advisor platform, a frame-relay-based network of 630 branches around the world plus call centers and data centers.. This contract will involve the provision of AT&T platforms and systems management technology and tools, implementation assistance, a global client support center, call center management services, and program management. The contract consolidates a variety of services currently delivered by other vendors. AT&T Solutions will also provide inbound and outbound voice services as well as underlying carrier and voice and data management facilities. Clearly, AT&T's global infrastructure and advanced network technology are key strengths in competition for a contract such as this.

EDS/Automakers Ltd.:
In this contract with Automakers Ltd., which is South Africa's Nissan manufacturer, EDS will manage and develop Automakers' information systems and will be paid based on the systems' performance and impact on Nissan profitability. EDS is transitioning 28 employees to EDS and installing a new computer network worth $1.2M. EDS will implement SAP R/3 software to support the replacement of Nissan's current dealer network and will provide LAN capabilities to its regional office.

HP/SmithKline Beecham:
HP will be responsible for keeping SmithKline Beecham's global WAN operating at maximum efficiency. HP's network services will include change and configuration management, fault management, performance management and optimization and network help desk. SmithKline will experience cost-savings by eliminating software-related network-management costs and training-related costs.

NETWORK MANAGEMENT KEY TO OTHER Q2 OUTSOURCING CONTRACTS

There were a number of outsourcing contracts awarded during the quarter that, while not primarily network management outsourcing contracts, nevertheless had a large network management component. As a member of the CSC-led Pinnacle Alliance, AT&T Solutions will be providing global network operations management for J. P. Morgan, which expects to save 15 percent of projected technology costs over the seven-year life of the $2B contract. CSC will operate and maintain Baker & Taylor's mainframe, network, telecommunications, applications and help-desk operations. Exhibit 4 provides a sampling of Second Quarter 1996 contracts with significant network management outsourcing components.

EXHIBIT 3

2Q OUTSOURCING CONTRACTS WITH SIGNIFICANT NET MANAGEMENT COMPONENTS

Vendor	Customer	Industry	Value ($M)	Length
AT&T	Disney Online	Telecom	NA	NA
CSC*/Pinnacle*	J P Morgan	Finance	2,000	7
CSC	U.S. Dept of Transportation	Federal	1,130	7
CSC	Baker & Taylor	Wholesale	63.4	7
EDS	Citicorp	Finance	250	NA
Unisys	British Telecommunications	Telecom	116	3
Unisys	Social Security Administr.	Federal	280	7
Alltel	Westamerica Bancorp	Finance	NA	NA

Source: INPUT's Outsourcing Database 1996

Although this is a small sample, it is nevertheless confirmation that contracts with a large network management component are often the large contracts of long duration. The available figures from the table above, when averaged, yield impressive contract parameters:

Insert 3a

PROFILE OF CONTRACTS WITH NET MANAGEMENT SERVICES	
Av Contract Size	$668 Million
Av. Contract Length	7.8 Years

FINANCE LEADS SECTORS OF OPPORTUNITY

Finance topped the list of industries in which network management was a major opportunity. AT&T won a $500M network management contract with Merrill Lynch and another with Mastercard International. Network Management is also a key component of CSC's Pinnacle Alliance's contract with J.P.Morgan, with the network management portion of the deal being executed by alliance member AT&T Solutions. And EDS' recent contract with Citicorp also includes a significant network management component. INPUT has forecast the market for network management outsourcing in the Banking and Finance market to grow at a rate of 30% CAGR to $1.8B in the U.S. over the next 5 years.

* CSC-led Pinnacle Alliance: ~~[illegible]~~, Andersen Consulting, AT&T Solutions, Bell Atlantic Network Integration

Exhibit 3 indicates the sectors offering significant network management opportunities during the Second Quarter 1996:

EXHIBIT 3

OPPORTUNITY SECTORS

Finance
Federal Government
Telecommunications
Process Manufacturing
Discrete Manufacturing

NETWORK MANAGEMENT OUTSOURCING VENDORS

There are a number of vendors successfully targeting this strong-growth segment of outsourcing. They are listed in Exhibit 5, below.

EXHIBIT 5

LEADING VENDORS

AT&T
CSC
EDS
Digital
H-P
Unisys
(add IBM/ISSC?, others?)

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Vol. VII, No. 4

July 1996

Second Quarter Network Management Outsourcing Contracts

Strong Growth Market

Analysis of INPUT's Outsourcing Database for the Second Quarter of 1996 indicates that Network Management Outsourcing is increasing, and that many of the very large contracts include network management outsourcing services as a key component. INPUT projects that the Network Management Outsourcing market will grow at a CAGR of 25% to reach $6.4B in the year 2000 (see Exhibit 1).

Market Drivers

Drivers of Network Management Outsourcing market growth include:

- Trend toward distributed computing
- Increasing network complexity and maintenance requirements
- Increasing dependence on networks for mission-critical activities
- Soaring support costs
- Globalization

Significant Q2 Contracts

A sampling of notable Network Management Outsourcing contracts won during the Second Quarter of 1996 appears in Exhibit 2, followed by a brief description of key contracts.

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Source: INPUT 1996 Outsourcing Database

All of these contracts reflect the influence of globalization, a key driver in the Network Management Outsourcing market. Several contracts are encapsulated in the following section.

Contract Briefs

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This is a multimillion dollar contract to design, build and support the management of a global transaction processing network for Mastercard so that it will be able to support credit and debit transactions in more than 30 countries. AT&T will support end-to-end network management and provide maintenance of customer premises equipment, as well as program and network engineering management. AT&T will leverage its WorldSource services and its global frame relay service. It will deliver services through its new Global Client Support Center in Durham, N.C., linked to regional centers in Singapore and Amsterdam. The contract is indicative of the need of financial players to develop strong electronic commerce capabilities in order to remain competitive in the Finance sector.

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Although this is a small sample, it is nevertheless confirmation that contracts with large network management components are often the large-sized contracts of long duration. The available figures from the exhibit above, when averaged yield impressive contract parameters:

Insert 3A

Finance Leads Sectors of Opportunity

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Exhibit 4 indicates the sectors offering significant network management opportunities during the Second Quarter 1996:

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